



STATE OF ARIZONA
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JOHN A. GREENE
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Circular Letter 1998-2

TO: All Service Companies, Motor Vehicle Service Contract Administrators, Insurance Industry Representatives, Insurance Trade Associations, Property & Casualty Insurers, And Other Interested Parties

FROM: John A. Greene
Director of Insurance

DATE: May 28, 1998

RE: Administration of Arizona's Service Company and Motor Vehicle Service Contract Administrator's Laws; Arizona Revised Statutes, Title 20, Chapter 4, Article 11

This circular letter clarifies the effect of the provisions of Arizona Revised Statutes, Title 20, Chapter 4, Article 11, governing the issuance of "service contracts."

A full understanding of the issues discussed in this Circular Letter requires consideration of several key definitions, including:

- *Service Contract:* A written contract for a prepaid, separately stated consideration to perform, over a fixed period of time or for a specified duration, services relating to the maintenance or repair of, among other things, "consumer product[s]", including motor vehicles. A.R.S. §§ 20-1095(2), (7) and (8).
- *Motor Vehicle Service Contract Program:* The documentation used in connection with the sale of service contracts by motor vehicle dealers. A.R.S. § 20-1095(5).
- *Service Contract Administrator:* An entity which agrees to provide contract forms, process claims and procure insurance for and on behalf of a motor vehicle dealer. A.R.S. § 20-1095(9).

- *Service Company*: Any person who performs or arranges to perform services pursuant to a service contract issued by that person. A.R.S. § 20-1095(7).
- *Mechanical reimbursement insurance*: An insurance policy issued to a motor vehicle dealer to insure the performance of a motor vehicle service contract to a consumer if the dealer or administrator becomes insolvent or ceases to do business. A.R.S. § 20-1095(4).

It has recently come to this Department's attention that certain motor vehicle service contract programs are not operating in compliance with these Title 20 provisions. The laws described in this circular letter apply to all service contract programs, notwithstanding any prior approval issued by the Department to a non-compliant program.

All Service Companies issuing motor vehicle service contracts (MVSC) and all service contract administrators ("Administrators") should note the following:

1. A party who issues a motor vehicle service contract which creates a direct contractual relationship between that party and a consumer is acting as a Service Company and must obtain a permit to act as a Service Company, unless expressly exempted by Title 20 from the requirement to do so. It is important to note that a party is not exempt from the requirement to obtain a Service Company permit merely because it self-administers its own motor vehicle service contract program rather than using the services of an Administrator.

2. If an Administrator has a direct contractual relationship with a consumer, it is acting as a Service Company rather than as an Administrator with respect to service contracts handled pursuant to this direct contractual relationship. Significantly, a party is acting in the capacity of an Administrator only when it performs the services described in A.R.S. § 20-1095(9) and is **not** a party to the MVSC.

3. A licensed Service Company may lawfully act as an Administrator for another licensed Service Company or motor vehicle dealer with respect to MVSCs issued by another Service Company or motor vehicle dealer.

4. Mechanical reimbursement insurance may be used to satisfy the financial responsibility requirements applicable to each motor vehicle service contract program pursuant to A.R.S. § 20-1095.06. If this option is selected, the policy must be issued to the dealer as the named insured, not the Administrator. A.R.S. § 20-1095(4). Likewise, if the surety bond option is selected, the bond should name the dealer, not the Administrator, as the principal.

5. A licensed Service Company may sell MVSCs through a motor vehicle dealer if the MVSC program has been approved pursuant to A.R.S. § 20-1095.06. See A.R.S. §§ 20-1095.02(C) and 20-1095.07(A).

6. A motor vehicle dealer may receive a fee, commission or other contingent remuneration for selling MVSCs without being licensed as an insurance agent if the contracts are sold on behalf of a licensed Service Company and the MVSC program has been approved by the Director.

7. Although an insurer licensed in Arizona may possess a certificate of authority to write property and casualty insurance in this state, the insurer may not issue or sell service contracts unless it has obtained a Service Company permit pursuant to A.R.S. § 20-1095, *et seq.* See A.R.S. §§ 20-107(A) and 20-113.

8. Pursuant to A.R.S. § 20-1095.02(A)(5), a Service Company is exempt from the provisions of A.R.S. § 20-1095, *et seq.* (except A.R.S. § 20-1095.09) to the extent it issues service contracts relating to consumer products specified in A.R.S. § 20-1095(A)(5) which it is also in the business of selling or servicing.

Based on our review of the activities taking place in the market, we estimate that most of the entities currently acting as Administrators must obtain a Service Company permit. We also believe that most of the entities now licensed as Service Companies do not require a Service Company permit in light of the exemption contained in A.R.S. § 20-1095.02(A)(5).

The Department of Insurance will treat all new applications consistently with the law described in this circular letter. Parties currently not in compliance with the law are encouraged to come into compliance with the law as described in this circular letter by December 31, 1998. After that date, parties who are not in compliance risk administrative action.

Any person with questions about this circular letter should direct them to Jack Curry at (602) 912-8466.